

**R E S O L U T I O N**

Resolution E-3929. Pacific Gas and Electric ("PG&E") requests Commission approval of a three-year physical tolling agreement beginning in 2005 through December 2007 with Duke Energy Marketing Americas ("Duke" or "DEMA"). PG&E's request is approved with modifications.

By PG&E Advice Letter ("AL") 2632-E, filed February 23, 2005.

---

**SUMMARY**

In AL 2632-E, PG&E seeks approval of a three-year physical tolling agreement beginning in 2005 through December 2007 with Duke. This resolution approves PG&E's proposal. While neither PG&E nor Duke requested expedited treatment of this advice letter, due to summer reliability concerns, we have processed this advice letter on an expedited basis. Finally, as the City of Morro Bay ("City") is not a market participant, this resolution requires that PG&E make available the advice letter in its entirety (including Appendices A through D) to the City once the City has signed a non-disclosure agreement as provided for in the modified protective order adopted in Rulemaking (R.) 01-10-024.

**BACKGROUND**

As explained in PG&E's advice letter filing, on October 11, 2004 Duke issued a Request For Bids (RFB) from qualified parties interested in purchasing the output from one or both of its Morro Bay Generation Units 3 and 4, 325 MW each, for up to three years beginning in 2005. On November 5, 2004, PG&E submitted non-binding three-year bids and was selected to the shortlist on November 15, 2004.

PG&E presented its proposed bid strategy to the Procurement Review Group on November 2, 2004, and details of the proposed transaction on December 14, 2004, and January 14, 2005.

## **NOTICE**

Notice of PG&E AL 2632-E was made by publication in the Commission's Daily Calendar. PG&E states that a copy of the Advice Letter, excluding the confidential appendices (Appendices A, C & D), was mailed to the service list for R.01-10-024 and non-market participants who are members of PG&E's Procurement Review Group in accordance with General Order 96-A, Section III, Paragraph G.

## **PROTESTS**

**PG&E AL 2632-E was timely protested by Coastal Alliance on Plant Expansion ("CAPE"), City and County of San Francisco ("CCSF"), and City of Morro Bay ("City") on March 15, 2005. On March 17, the California Independent System Operator Corporation ("CAISO") filed a letter of support for PG&E's proposed contract with Duke.**

The City and County of San Francisco's (CCSF) only comment on PG&E's proposed agreement relate to the need for PG&E to be mindful of its requirements imposed by Assembly Bill (AB) 117 to direct the investor-owned utilities ("IOUs") that energy procurement forecasts be made with community choice aggregation ("CCA") departing load in mind. CCSF reminds the commission that as it is currently crafting rules to comply with AB117 and its prohibition on cost shifting to utility bundled service customers, it is prudent for PG&E to plan for decreased energy procurement needs to serve San Francisco.

The California Independent System Operator ("CAISO") filed a letter of support for the proposed agreement, noting that the "...proposed transaction appears to provide PG&E with significant benefits, including the acquisition of capacity eligible for meeting its resource adequacy obligation..." in addition to deferring the retirement of Morro Bay Generation Units 3 and 4.

The Coastal Alliance on Plant Expansion ("CAPE") protests the AL because "...the facility does not currently possess authority to discharge heated cooling water through its outfall and [because] Duke has shown no present intent to move forward with its application for a new National Pollutant Elimination

Discharge System (“NPDES”) permit for Units 3 and 4.”<sup>1</sup> CAPE explains that Duke has filed an application for certification of a replacement plant with the California Energy Commission (“CEC”) for a new facility located on another portion of the site consisting of two new gas-fired turbines capable of generating up to 1,200 MW. Duke’s existing NPDES expired in 2000 and is currently on “administrative extension” by the Regional Water board with respect to its prior NPDES permit for the existing facility. CAPE further notes that Duke currently has yet to receive a new NPDES permit either for the new facility or the existing units. Further, Duke has not brought its facility into compliance with new regulations issued by the Environmental Protection Agency in 2004.

CAPE requests that if the commission does not reject the Agreement, it should require the terms of the agreement to be disclosed and the matter set for formal hearing.

The City of Morro Bay protests that PG&E is seeking approval of the proposed agreement with Duke through an advice letter process rather than formal hearings. Specifically, the City argues that: (1) PG&E did not properly serve or give notice of the advice letter, (2) the request violates the City’s statutory duty to protect sensitive “Tidelands Trust” property, (3) the advice letter contains material errors and omissions – specifically with respect to obligations owed by Duke to the City for ocean outfall, franchise obligations and natural gas surcharge fees, and (4) the proposed agreement is unjust, unreasonable or discriminatory.

The City’s protest is similar to CAPE’s with respect to the Tidelands Trust Property and the outfall lease. Both argue that the City’s responsibilities to protect the sensitive Tidelands Trust Property require an outfall lease with Duke that has yet to be renewed. A previous 50-year outfall lease expired in November 2004. The City questions whether the agreement for the output of the facilities’ power would require environmental review pursuant to the California Environmental Quality Act (“CEQA”).

With respect to costs underlying the agreement, the City is concerned that the agreement may not protect the continued payment to the City of the electricity

---

<sup>1</sup> Protest by CAPE, p. 1

and gas franchise agreements between the City and PG&E, which generate as much as \$4 million annually to the City general fund. Further, the City is “concerned that the agreement does not adequately account for or fund Duke’s obligation to upgrade and modernize the facility, including Duke’s obligation to remove the smoke stacks.”<sup>2</sup>

As such, the City requests that the advice letter not be kept confidential and that the matter be resolved in a formal proceeding rather than through an advice letter process.

PG&E filed response to the protests on March 22, 2005. In its response, PG&E attaches a letter from Duke responding to the City’s and CAPE’s protest of the advice letter.

In response to CCSF’s protest, PG&E maintains that it is premature to remove potential CCSF CCA load from its load forecast at this time, or to conclude that Morro Bay is not needed to serve CCSF load. PG&E properly explains that until there is a conclusive decision by the San Francisco Local Agency Formation Commission, PG&E continues to have an obligation to serve all of its customers, including those of CCSF.

With respect to protest by the City of Morro Bay, PG&E clarifies that its agreement with Duke is a commercial agreement which does not change or alter existing agreements or obligations either PG&E or Duke have with the City. Except for dispatch instructions, which PG&E will be responsible for under the agreement, Duke continues to be responsible for the operations and maintenance of the units. For example, PG&E states that “the agreement does not modify the existing electric and gas franchise fee obligations from PG&E to Morro Bay, nor does it modify obligations pertaining to PG&E’s gas rate schedule G-SUR.”<sup>3</sup>

With respect to environmental impacts, PG&E notes that its agreement with Duke is not a “project” for the purposes of CEQA, but continues an existing use of an existing facility which requires no review.

---

<sup>2</sup> Protest of the City of Morro Bay, p. 5

<sup>3</sup> Response of PG&E, p. 3

Finally, PG&E notes that it had served the advice letter in accordance to General Order 96-A to the service list in R.01-10-024 and to its Procurement Review Group.

No protests were filed from any members of the Procurement Review Group.

## **DISCUSSION**

**There are essentially five issues protested: (1) the need for consideration of departing load; (2) the need for an outfall lease; (3) the need to continue existing franchise fees obligations; (4) the need to disclose the agreement and not keep it confidential; and (5) the need for formal hearings. This resolution finds that it is premature to take into account CCSF CCA load, the agreement is approved contingent on resolution of noted agreements between the City and Duke, nothing in this agreement excuses PG&E from its obligations to the city, and the advice letter will only be kept confidential for market participants. Finally, we find that there is no need for formal hearings.**

### **Departing Load:**

With respect to CCA departing load issues raised by CCSF, we agree that the commission, and PG&E, need to be mindful of potential departing load in making long-term procurement decisions. CCSF accurately points out that in the CCA proceeding, the commission, with CCSF's active participation, is currently developing rules to comply with AB117. AB117 created the Community Choice Aggregation program and required that the commission establish a mechanism to prohibit costs being shifted onto utility bundled service customers as a result of CCA. CCSF's concern that absent considering and taking into account the potential loss of CCSF CCA departing load, costs associated with the PG&E/Duke agreement could be imposed on CCSF customers. While we share that concern, we note that the contract in question is for a three-year period to end in 2007. This is a short enough time-frame to permit CCSF to finalize decisions on CCA formations while still permitting PG&E to enter into this agreement without jeopardizing CCSF's CCA intentions. Further, comparing the notional cost of the Duke's agreement with offers PG&E received from its

intermediate-term RFO, the cost of the Morro Bay units is the cheapest among others.<sup>4</sup> We agree with PG&E that until there is more conclusive decisions made on behalf of CCSF regarding its authority to enter into a CCA arrangement, PG&E's obligations as an energy provider require it to continue to procure on behalf of its existing customer base.

**Outfall Lease:**

With respect to the outfall lease, we note that there is wide disagreement between the City and Duke on whether Duke is currently authorized to operate under an expired lease agreement with the City. Duke acknowledges that its 50-year lease agreement expired on November 14, 2004. However, it believes that its current arrangement permits it to operate the plant on a month-to-month basis. Not surprisingly, the City believes that Duke is operating unlawfully.

While we cannot ignore the fact that there is legal dispute over the need for an existing outfall lease, we note that the dispute is between the City and Duke. PG&E's agreement with Duke includes provisions to make the contract null and void should the facility be unable to lawfully operate.<sup>5</sup> As such, we will approve the agreement contingent on the resolution of the lease issue in a manner that allows Duke to lawfully operate the units.

**Franchise Fees Obligations:**

With respect to existing franchise fees obligations, PG&E has stated in its response to the protest of the City that it will continue to honor its obligations and that the agreement does not modify such obligations. We agree. We find nothing in the agreement to suggest that PG&E is stepping away from its current obligations. In fact, the Master Power Purchase Agreement addresses existing obligations between parties other than Duke and PG&E. We will hold PG&E to their response and ask the City to inform us if PG&E's obligations are not met as a direct result of this agreement.

**Confidentiality and Need for Formal Hearings:**

---

<sup>4</sup> AL 2632-E, Confidential Appendix D, p.16

<sup>5</sup> AL 2632-E, Confidential Appendix A, p. 12

Finally, with respect to confidentiality protection and the need for formal hearings, the City argues that material errors were omitted that if revealed, would require formal hearings. In part, the City's concerns rest on the fact that the appendices to the advice letter were filed confidentially. In its advice letter, PG&E states that,

The portions of this advice letter so marked Confidential Protected Material are in accordance with the May 20, 2003, Modified Protective Order in R.01-10-024 Regarding Confidentiality of Pacific Gas and Electric Company Power Procurement Information. As required by that Order, reviewing representatives of market Participating Parties will not be granted access to Protected Material, but will instead be limited to reviewing redacted versions of documents that contain Protected Material.<sup>6</sup> (AL, p.4)

Except for Appendix B (Duke's Request for Bids), PG&E seeks to keep all other appendices confidential, which include the executed agreement.

The protections adopted in R.01-10-024 were done so to protect the utilities, and utility ratepayers, from being harmed from releasing contract terms and prices prematurely. As the utilities were engaging in short-, medium- and long-term procurement through 3<sup>rd</sup> parties, the need to keep confidential aspects of the agreements became vital so as not to expose their energy/capacity needs and undermine future competitive bid processes. However, the commission was clear that the intent of the protective orders was to protect the interests of ratepayers.

Further, the only party seeking contract information is the City of Morro Bay. While the City is not a current member of PG&E's procurement review group, it is nonetheless a non-market participant. As such, our non-disclosure agreement as adopted in the modified protective order in our procurement rulemaking adequately protects the interests of PG&E's ratepayers. As such, we find that any non-market participant, including the City, can have access to the confidential appendices of the advice letter provided they first sign a non-

---

<sup>6</sup> AL 2632-E, p. 4

disclosure agreement pursuant to the Modified Protective Order adopted in R.01-10-024.

## **COMMENTS**

Public Utilities Code section 311(g)(1) provides that this resolution must be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission. Section 311(g)(2) provides that this 30-day period may be reduced or waived upon the stipulation of all parties in the proceeding:

The 30-day period may be reduced or waived in an unforeseen emergency situation, upon the stipulation of all parties in the proceeding, for an uncontested matter in which the decision grants the relief requested, or for an order seeking temporary injunctive relief.

Energy Division requests that the 30-day comment period for this resolution be reduced because a delay in approving the contract may prevent the facility from being available and online by June 2005. We are concerned that the reliability of the electrical grid may be compromised this summer if we do not ensure that there are adequate resources available to meet peak demand.

Comments are due April 4, 2005. No reply comments will be accepted.

## **FINDINGS**

1. By AL 2632-E, PG&E seeks approval of a three-year physical tolling agreement beginning in 2005 through December 2007 with Duke's Morro Bay Generation Units 3 and 4.
2. PG&E requests confidentiality for the terms of its agreement.
3. The City of San Francisco, the Coastal Alliance on Plant Expansion, and the City of Morro Bay filed timely protests on March 15, 2005.
4. The California Independent System Operator filed a letter of support on March 15, 2005.
5. PG&E filed timely responses to the protests on March 22, 2005.
6. The City's protest regarding existing obligations by PG&E owed to the City are not altered or changed by this agreement.



April 7, 2005

7. Duke's 50-year outfall lease expired on November 14, 2005.
8. The City and Duke have are in disagreement regarding the lawful operation of the units pursuant the outfall lease.
9. The City's protest regarding the confidentially aspect of AL 2632-E should be granted.
10. There is no need for the commission to proceed with a formal hearing.

**THEREFORE IT IS ORDERED THAT:**

1. The request of Pacific Gas & Electric Company (PG&E) for Commission approval of a three-year tolling agreement with Duke's Morro Bay Units 3 and 4 is approved contingent on the resolution of the necessary agreements between the City and Duke as outlined in the last paragraph of the Master Power Purchase Agreement.
2. Consistent with the Protective Order in R.01-10-024, PG&E will make available the advice letter in its entirety (including all appendices) to any non-market participant (including the City of Morro Bay) once they have signed a non-disclosure agreement as provided for in the modified protective order adopted in Rulemaking (R.) 01-10-024.

This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed and adopted at a conference of the Public Utilities Commission of the State of California held on April 7, 2005; the following Commissioners voting favorably thereon:

---

STEVE LARSON  
Executive Director

April 7, 2005

Item 42, ID#4449

March 29, 2005  
RESOLUTION E-3929

Commission Meeting

April 7, 2005

TO: PARTIES TO PACIFIC GAS & ELECTRIC ADVICE LETTER NO 2632-E

Enclosed is draft Resolution Number E-3929 of the Energy Division. It will be on the agenda of the Commission meeting of April 7, 2005. The Commission may then vote on this Resolution or it may postpone a vote until later.

When the Commission votes on a draft Resolution, it may adopt all or part of it as written, amend, modify or set it side and prepare a different Resolution. Only when the Commission acts does the Resolution become binding on the parties.

Parties may submit comments on the draft Resolution.

An original and two copies of the comments, with a certificate of service, should be submitted to:

Jerry Royer  
Energy Division  
California Public Utilities Commission  
505 Van Ness Avenue  
San Francisco, CA 94102

A copy of the comments should be submitted to in hard copy and by email:

Manuel Ramirez  
Energy Division  
California Public Utilities Commission  
505 Van Ness Avenue  
San Francisco, CA 94102  
[mzr@cpuc.ca.gov](mailto:mzr@cpuc.ca.gov)

April 7, 2005

Any comments on the draft Resolution must be received by the Energy Division by April 4, 2005 by 5pm. Those submitting comments must serve a copy of their comments on 1) the entire service list attached to the draft Resolution, 2) all Commissioners, and 3) the Director of the Energy Division, on the same date that the comments are submitted to the Energy Division.

Comments shall be limited to five pages in length plus a subject index listing the recommended changes to the draft Resolution, a table of authorities and an appendix setting forth the proposed findings and ordering paragraphs.

Comments shall focus on factual, legal or technical errors in the proposed draft Resolution. Comments that merely reargue positions taken in the advice letter or protests will be accorded no weight and are not to be submitted.

No replies comments will be accepted.

Late submitted comments or replies will not be considered.

Manuel Ramirez  
*Energy Division*

*Enclosure: Service List*

CERTIFICATE OF SERVICE

**CERTIFICATE OF SERVICE**

I certify that I have by mail this day served a true copy of Draft Resolution E-3929 on all parties in these filings or their attorneys as shown on the attached list.

Dated March 29, 2005 at San Francisco, California.

---

*Jerry Royer*

**NOTICE**

Parties should notify the Energy Division, Public Utilities Commission, 505 Van Ness Avenue, Room 4002 San Francisco, CA 94102, of any change of address to insure that they continue to receive documents. You must indicate the Resolution number on the service list on which your name appears.

April 7, 2005

Brian Cherry, Director Regulatory Relations  
Pacific Gas & Electric  
77 Beale Street  
P.O. Box 770000  
San Francisco, Ca 94117

Deborah Sivas  
Earthjustice Environmental Law Clinic at Stanford  
553 Salvatierra Walk  
Stanford, Ca 94305

Joseph P. Como, Deputy City Attorney  
City and County of San Francisco  
1 Dr. Carlton B. Goodlett Place, Room 234  
San Francisco, Ca 94102

Grant A. Rosenblum, Regulatory Counsel  
California Independent System Operator  
151 Blue Ravine Road  
Folsom, Ca 95630

Colin L. Pearce  
Duane Morris LLP  
One Market, Spear Tower, Suite 2000  
San Francisco, Ca 94105

Rob Schultz, City Attorney  
City of Morro Bay  
955 Shasta Avenue  
Morro Bay, Ca 93442